

# **CAPITAL PLANNING ADVISORY BOARD**

## **Minutes of the 4th Meeting of the 2005 Calendar Year**

**September 23, 2005**

The 4th meeting of the Capital Planning Advisory Board (CPAB) was held on Friday, September 23, 2005, at 10:00 AM, in Room 327 of the Capitol. Senator Jack Westwood, Co-Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Jack Westwood, Co-Chair; Representative Perry Clark, Co-Chair; Senator David Boswell; Representative Ron Crimm; Paul Gannoe; Bill Hintze; William May; Jason Nemes; Norma Northern; Laurel True; Garlan Vanhook; and Melinda Wheeler.

Guests: Joe Wolford, ESPC Program Coordinator, Finance and Administration Cabinet.

LRC Staff: Pat Ingram, Mary Lynn Collins, and Debbie Rodgers.

Representative Crimm's motion to approve the minutes of the August 26 meeting was seconded by Mr. Hintze and passed by voice vote.

Senator Westwood asked CPAB Staff Administrator Pat Ingram to review the four information items included in the members' folders.

Ms. Ingram said the first item was a resolution passed by the Kentucky Library Association and forwarded to the Board in support of the proposed project to construct an addition to the Department for Libraries and Archives (DLA) building. The addition would be used for archival records storage. Also included was a memorandum from State Librarian James Nelson announcing a moratorium on records transfers due to lack of space at the DLA building.

The second information item reviewed by Ms. Ingram addressed the various proposals for biosafety laboratories that have been included in the capital plans of the postsecondary institutions. She said the University of Louisville (UL) has now received a federal grant for a portion of the cost of its proposed Biosafety Level 3 (BSL-3) facility, the University of Kentucky has deleted its proposal to renovate space for a BSL-3 lab, and Murray State University continues to plan for a section of its proposed Breathitt Veterinary Center replacement facility to be constructed to BSL-3 standards. Noting his

involvement in plans for development of the UL Shelby Campus, which is to be the site of the lab, Representative Crimm said it will be a tremendous boost to the research efforts of the state. It will help the universities and the medical facilities as well as creating high tech jobs.

Ms. Ingram said the third information item reports on the Finance and Administration Cabinet's use of its FY 2005/06 Maintenance Pool. Because this pool is part of the larger Statewide Repair, Maintenance and Replacement Pool Fund that was authorized from state bonds in the current budget, the funds must be used for more major projects with a useful life that will match the 20-year life of the bonds. For example, the Cabinet will use \$2.3 million of its \$3.75 million pool for a single project to renovate the Jones Building. This is a change from the traditional use of maintenance pools that have been cash funded and used for smaller projects. Ms. Ingram said the Board has supported funding for the cash-funded maintenance pools as a high priority because they could be used for smaller projects and, thereby, head off the need for larger, more costly maintenance projects in the future.

The final information item reported by Ms. Ingram was a report on the status of major state-funded projects authorized in the current (2004-06) budget. She said since the budget had just recently been enacted, little status information was available to report at the July meeting. There has now been some action on almost all of the projects, with most being in the consultant selection or early design phases.

Senator Westwood thanked Ms. Ingram and said there is one more information item to be provided in the form of a presentation on Energy Savings Performance Contracts (ESPCs). He said the Board has historically supported and encouraged the use of ESPCs as a means of saving on energy costs and a way to undertake needed projects that can appropriately be financed using this approach. He introduced Joe Wolford, ESPC Program Coordinator in the Finance and Administration Cabinet, to make the presentation.

Mr. Wolford said ESPCs can be viewed from different perspectives - agencies look at them as a way of procuring capital improvements and the Office of Financial Management sees them as a financing method for capital construction, while the Division of Energy considers them as a self-funding means of energy savings. Mr. Wolford said an ESPC is a performance-based contract whereby an energy service company is hired to provide facility improvements. Those facility improvements are paid for from energy and operational savings, which are guaranteed to the Commonwealth by the company. The projects work as lease-purchase agreements and third-party financing is used.

Mr. Wolford said there are 12 ESPCs currently under contract by state agencies and postsecondary institutions. The agencies are the Department of Military Affairs (11 facility locations), the Department of Corrections (three sites), the Transportation

Cabinet, and the Finance Cabinet (three separate contracts/projects). The postsecondary institutions are the Kentucky Community and Technical College System (four campuses), Kentucky State University, Morehead State University, Murray State University, Northern Kentucky University, and Western Kentucky University. He added that development is underway for projects of the Kentucky State Fair Board, the Cabinet for Health and Family Services, and the Education Cabinet/Department for Workforce Investment. The Education Cabinet project will be coupled with another construction project in order to prepare vacant space in the DES building at Sixth and Cedar in Louisville for occupancy by state employees. In summary, Mr. Wolford said the state has undertaken \$50 to \$60 million in ESPC projects to date.

In response to Senator Westwood's question, Mr. Wolford said for each project there are guaranteed savings and often the companies underestimate the savings, so typically the Commonwealth has savings in excess of the estimates.

Mr. Hintze noted that the purpose of the ESPC program has changed significantly. It was initially advocated solely as a means of realizing energy savings, which is a desirable goal in and of itself. It has now also become another approach for agencies to use to undertake ordinary maintenance and upgrade projects related to items such as lighting, windows, and HVAC systems, which are usually funded from maintenance pools if they receive funding at all. He said having this additional way to address infrastructure needs has been an important, and unintended consequence of the program, and he expects its use to be expanded.

Mr. True asked if the Commonwealth would continue to receive benefits beyond the six-year payback term from the Transportation Cabinet project for LED retrofits of lights. Mr. Wolford said the savings will extend beyond that period. He added that energy costs savings only, not operational savings, are calculated in the payback.

After thanking Mr. Wolford for his presentation, Senator Westwood noted that the Board would continue work on development of the *2006-2012 Statewide Capital Improvements Plan* beginning with a few remaining policy recommendations, then moving to the project recommendations. He asked Ms. Ingram to begin this discussion.

Ms. Ingram first reviewed an agenda item that provided an overview of the proposed content and organization of the Plan. She explained that, consistent with previous plans, the 2006-2012 plan would contain an Executive Summary and sections for Policy Recommendations, Project Recommendations, and the Status of Major State-Funded projects, a Comprehensive Listing of Proposed Projects (2006-08, 2008-10, 2010-12), and Appendices (KRS Chapter 7A and the reports submitted by the Council on Postsecondary Education and the Commonwealth Office of Technology). Ms. Ingram also said the brief descriptions of all projects proposed by the agencies would be posted on the CPAB webpage.

Ms. Ingram next reviewed the two new proposed recommendations being presented today. The first was based on the Board's discussion at the last meeting about the possible need for a review of the state's debt policies and practices. She noted there have been a lot of changes since the last review was undertaken about 15 years ago. Those changes include an expansion in the nature of projects that are financed from bonds, an increase in the long-term funding commitments by the state that do not involve the issuance of bonds, and recent requests and proposals to identify alternative ways of funding postsecondary education projects. She presented the following recommendation: That the 2006 General Assembly establish a task force composed of representatives of the Executive and Legislative branches to review Kentucky's debt issuance processes and approaches to debt capacity. Subjects to be addressed by the task force should include, but not be limited to, the approach used to determine the amount of debt that should be issued by the Commonwealth, the type of projects for which debt is the appropriate funding mechanism, structuring guidelines for debt including appropriate terms and covenants, and alternatives to address the capital needs of the postsecondary institutions.

In response to Senator Westwood's question, Representative Clark confirmed that the intent is for the task force to include an examination of how alternative approaches to funding university projects would impact bonding capacity.

Staff was directed to finalize the recommendation as presented.

Ms. Ingram said the next proposed recommendation is new only in that it has not been discussed yet during the current planning process, but the recommendation has been made consistently in previous plans. It addresses the need to replenish and adequately fund the Budget Reserve Trust Fund (BRTF). Ms. Ingram said KRS 48.705 speaks to maintaining a balance in the Reserve equal to 5 percent of General Fund receipts and that the rating agencies have indicated an amount equal to 3 to 5 percent of revenues demonstrates a "best effort" to prepare a state for fiscal uncertainties. With amounts to be deposited from the FY 2004/05 surplus pursuant to limits imposed by the budget bill, Kentucky's BRTF will be at 1.5 percent of budgeted revenues for FY 2005/06. The following recommendation was presented: That the Governor and General Assembly place a high priority on replenishing the Budget Reserve Trust Fund as quickly as possible to a level that represents 3 to 5 percent of General Fund revenues.

Representative Crimm asked if there are restraints on how moneys in the budget reserve can be used. Mr. Hintze said the statute that establishes the BRTF is narrow. The Fund can only be accessed when there is an officially declared revenue shortfall where receipts are not coming in at the level budgeted for expenditure by the General Assembly. Mr. Hintze then explained that the BRTF differs from the General Fund surplus. The surplus is extra money above what was budgeted, and it can be used for broader, more discretionary purposes. The 2005 General Assembly specified five uses for the 2004-05

surplus including replenishing the BRTF to a maximum level of 1.5 percent of annual revenues.

Senator Westwood asked what the advantage would be in increasing from the current 1.5 percent to having 3 to 5 percent of revenues in the BRTF. Mr. Hintze said following the authorization of a record \$2 billion in debt by the 2005 General Assembly, Kentucky was on "shaky ground" and was "extremely fortunate to hang on to" its credit rating. He said at that time the BRTF was miniscule and while the increase to 1.5 percent is an improvement, it is still not a respectable level of funding. An adequate BRTF provides a hedge against an economic downturn or emergencies with significant costs. Mr. Hintze said having 3 percent of revenues in the BRTF could put Kentucky closer to what other states have rather than being on the low end as is now the case. He said it is unfortunate that the current budget capped the amount that could go into the BRTF this biennium. If the reserve was already at the 3-5 percent level, a cap would be desirable since the need would be only to maintain or replenish it, not to continue adding to it.

Senator Boswell noted that he has introduced legislation that would put revenues into the Budget Reserve Trust Fund.

CPAB staff was directed to finalize the recommendation as presented.

Ms. Ingram said the next two recommendations were revisions to items considered at the last meeting. The first addressed state information technology and services and was based on the recommendations presented by the Commissioner of the Commonwealth Office of Technology. The Commissioner had asked for the support of the Board in three areas - the consolidation of information technology (IT), the establishment of a pool for information technology upgrades and replacements, and the application of consistent management practices. The following recommendation was presented: That the Board endorse efforts of the Commonwealth Office of Technology to improve the delivery of information technology in state government through the consolidation of operations and services and through the application of consistent project management practices, and that the Board also endorse further review and development of an approach and funding for agency information technology upgrades and replacements such as through the establishment of a maintenance or infrastructure pool option. Periodic reports on this effort should be submitted to the CPAB as this review and development proceed.

Ms. Ingram explained the reason for the two-part recommendation. She said endorsement of IT consolidation and project management practices was consistent with the Board's understanding of the role assigned to COT. Endorsing further review and development of an approach for IT upgrades and replacement recognizes that COT itself indicates it has not fully developed or finalized its proposal in this regard.

Noting that COT Commissioner Inman had said consolidations would be done "where appropriate" upon evaluation of the particular situation, Mr. Hintze said this is a good recommendation. He added that the requirement for periodic reports to the Board is also good since more attention needs to be given to this area of increasing importance and cost to the state.

Senator Westwood noted that at the Appropriations and Revenue Committee meeting on September 22, Education Commissioner Wilhoite had reported that the Department of Education and the schools have significant IT needs. Senator Westwood suggested that maybe all IT needs (schools and state government) should be addressed through a consolidated approach.

CPAB staff was directed to finalize the recommendation on state information technology operations and services as discussed.

The final policy recommendation was a revision of the proposal discussed at the last meeting regarding alternatives to incarceration. Ms. Ingram said, as directed by the Board, the proposed recommendation had been strengthened to specifically call for increased funding for programs with documented savings that provide alternatives to incarceration or reduce recidivism. Additional information on various existing program options was also included in the background material, as was the conclusion from a recent Law Journal article written by University of Kentucky Professor Robert Lawson, which analyzed the reasons for Kentucky's increasing prison population.

Ms. Ingram said after reviewing the revised recommendation included in the mailout to members, Judge Wehr had proposed some additional language. Ms. Ingram read the following recommendation as proposed by Judge Wehr: That the Executive, Legislative, and Judicial Branches should take actions to identify and provide alternatives to incarceration and adequate treatment options, consistent with public safety and victims' rights, that could reduce the prison population growth and the attendant need for the construction of new facilities. (Options might include public or private sector programs, changes to sentencing guidelines, and more substance abuse treatment programs for those already incarcerated.)

The proposal further recommended that the 2006 General Assembly increase funding for programs with documented savings that provide alternatives to incarceration or reduce recidivism, such as drug courts, community corrections programs, and substance abuse programs. This would allow our present prison beds to be used for the serious cases which require incarceration.

CPAB staff was directed to finalize the recommendation as presented.

Moving to the discussion of project recommendations for inclusion in the *2006-2012 Statewide Capital Improvements Plan*, Ms. Ingram noted that the Board has generally included recommendations for two categories of projects - projects involving state funds and projects to be financed entirely from other than state funds. She explained that the background for the recommendation on projects to be financed from state funds provided a summary of the state funding needs reflected in the Executive Branch agency plans and in the Judicial Branch plan. The background also noted that in making its project recommendations, the Board has traditionally emphasized that - as a planning body - its focus should be on the priority and need to be addressed, rather than the specific details of each project. Ms. Ingram said the potential recommendation continues that approach.

The introduction to the recommendation states that the Board believes good stewardship of assets acquired with revenues from the taxpayers requires that those assets be adequately maintained in order to continue providing services to Kentucky's citizens, and goes on to state that the Board also recognizes there are instances in which it is appropriate and necessary to acquire or construct new facilities or systems. The recommendation addresses both needs. It states that as its highest priority for state funds in the 2006-08 budget, the Board recommends funding for construction to protect investment in plant (maintenance) as follows: appropriations for the Agency Maintenance Pools should be from a source that will allow these pools to be used for their historical purposes of financing minor project needs; a Postsecondary Education Matching Funds Pool for Maintenance should be appropriated to the Council on Postsecondary Education with the allocation of the state funds by the CPE requiring a match of agency funds from the budget of the recipient institution; amounts should be appropriated to the Capital Construction and Equipment Purchase Contingency Account and the Emergency Repair, Maintenance, and Replacement Account to allow these two statutory funds to be used for the purposes specified in KRS Chapter 45; and funding for the ongoing State-Owned Dam Repair Program should be appropriated consistent with the requirements of KRS 151.291 to address needs documented for 2006-08 by the Environmental and Public Protection Cabinet.

The recommendation goes on to state that consistent with its long-standing position that the Commonwealth should reduce the amount of office space it leases from private vendors in Franklin County, the Board recommends the "Renovate State Office Building - Phase 3" project in order to complete the work necessary to make this facility available to relocate state employees from leased into state-owned space. The recommendation also calls for the Board to develop lists of specific project recommendations in three areas - major maintenance projects costing \$400,000 or more each, information technology, and new construction. Finally, it states that the Board traditionally does not make recommendations on the individual grant and loan programs that provide assistance to non-state entities, but has encouraged that appropriate funding

be provided particularly to those programs where state funds can be used to leverage federal funds.

Regarding the project listings, Ms. Ingram explained that, as has been done previously, the proposal is for each member to identify a certain number of projects in each category - major maintenance (15), other construction (15), and information technology (10). Those member recommendations would be compiled into the lists to be inserted in the appropriate sections of the recommendation. She said generally projects listed by only one or two members are dropped from the listing.

Representative Clark said this seems to have worked well in the past, and there appears to be a general consensus to use the same approach again. He asked staff to proceed with providing the project lists from which members would make their selections.

Ms. Northern asked if the four items listed first would be the top priorities (agency maintenance pools, CPE matching pool, Contingency and Emergency funds, and State-Owned Dam Repair). Ms. Ingram said the recommendation states that, overall, maintenance is the highest priority, and these are items identified in that category, but a priority ranking is not necessarily assigned to each individually.

Ms. Ingram next presented the final recommendation which addressed projects that would be financed 100 percent from other than state funds. She noted that rather than naming specific projects, the draft listed some items decision-makers should consider in authorizing such projects. It stated that in authorizing projects to be financed 100 percent from other than state funds and for which the other funds may be used for discretionary purposes, a high priority should be assigned to projects to address life/safety and deferred maintenance needs for which state funds were not provided. The recommendation then stated that in authorizing any projects to be financed 100 percent from other than state funds, the following factors should also be reviewed thoroughly: 1) Will the project require the expenditure of significant additional state funds for its operations and maintenance? 2) Will the project commit the state to fund significant costs to complete the project after the available other funds have been expended? 3) Are there any programs or operations also financed by the proposed fund source that would be jeopardized by the use of the funds for a capital project?

Mr. Hintze noted that while restricted, federal, and “other” funds are described as not being state funds for purposes of the Board’s recommendation, those fund sources are subject to appropriation and considered to be state funds in the biennial budget process.

CPAB staff was directed to finalize the recommendation on projects that would be financed 100% from other than state funds as presented.



There being no further business to come before the Board, Representative Crimm's motion to adjourn was seconded by Senator Boswell, and the meeting was adjourned at 11:12 AM.